

General Principles for the Use of

Parent Company Guarantees and Performance Bonds

This short paper is intended to describe the general principles to be applied in the use of Parent Company Guarantees and Performance Bonds with offshore oil and gas contracts. It has been prepared by the Standard Contracts Committee.

It should be noted that Parent Company Guarantees and Performance Bonds serve different, if related, purposes: the former are intended to ensure that contracts are fully performed, i.e. that the necessary resources will be provided and the whole enterprise is committed to ensuring such full performance; the latter are a means of providing financial recompense, in the event of a failure by a contractor or supplier, so that the client may recover some or all of his loss and/or may make and pay for alternative arrangements to complete the work in question.

It should be further noted that Parent Company Guarantees are contingent liabilities on the balance sheets of parent or holding companies, while Performance Bonds are direct charges on the balance sheets of contractors and suppliers, thus affecting their liquidity and banking covenants. As such, Performance Bonds, if large or numerous, may affect a contractor's or supplier's ability to conduct their business properly.

i) Parent Company Guarantees

Parties -- the Parties to a Parent Company Guarantee (PCG) will normally be the Client (but not the entire Client Group) and the Guarantor which will either be the ultimate holding company of the contractor/supplier ("Contractor" used hereinafter) or an intermediate holding company (if acceptable to Client).

Contract -- there must be a specific reference to the contract that the Guarantor is guaranteeing. Also, the PCG should be drafted in a manner so as to accommodate any changes to the contract negotiated between the Contractor and the Client.

Irrevocable -- the PCG should be irrevocable.

Assignment -- the question of assignment should be addressed in the PCG to cover circumstances where the contract is assigned by the Client or Contractor to a third party.

Duration -- the duration would normally be for the life of the contract being guaranteed, although it may be for a defined term.

Law -- the PCG must state the law under which it is governed. This is recommended to be the same as the law which governs the performance of the contract.

Notice -- notice provisions must be recorded in the PCG.

Extent of guarantee -- it should be made clear in the PCG that the aggregate limit of liability of the Guarantor under the guarantee should not exceed the limit of liability of the Contractor under the contract. In addition, the PCG should not create obligations and liabilities in excess of those which are incumbent on the Contractor under the contract. Normal remedies available under the contract should be applied, but not necessarily exhausted, before any use is made of a PCG.

Third party rights -- third party rights should be excluded under the guarantee, subject to any provisions under applicable law.

Change of ownership -- the Parties should assess the question of an outstanding PCG in the event that the Contractor is sold. It may be appropriate for the new holding company to issue a replacement PCG, if this is acceptable to the Client, in which case the original PCG may then be cancelled.

Client's guarantee -- the Contractor should consider asking for a PCG from the Client's holding company, where this would be appropriate.

ii) Performance Bonds

Parties -- a Performance Bond (PB) is issued by a reputable bank or insurance company (the Guarantor) acceptable to the Client in favour of the Client (but not the Client Group) to guarantee the performance of a contract up to a stated financial limit.

Contract -- a PB must specifically relate to the performance of the contract concerned. The PB should be drafted in a manner so as to accommodate any changes to the contract negotiated between the Contractor and the Client.

Value -- the maximum value of the bond must be specifically stated in the PB, whether as a sum of money or as a percentage of the contract price at the start of the contract (such value may be drawn in tranches if specifically stated). There may be a provision in the contract to require the Contractor to increase the value of the PB if the scope of work increases significantly. There may also be a provision in the contract to allow a reduction in the value of the PB at the commencement of the warranty period.

Expiry Date -- the expiry of a PB should normally be stated as a specific date. It should not normally be referenced to an uncertain date under the contract (e.g. to a particular event), unless this is combined with a "drop dead" date. The Client should be required within the contract's provisions to return an expired PB to the Contractor.

Irrevocable bond -- a PB should be irrevocable.

Conditional bond -- banks are unlikely to accept a conditional PB, because they do not like having to interpret the quality of the Contractor's performance under a contract. In addition, some major clients will not use conditional PBs.

Calling a bond -- the notice provided to the Guarantor for the calling of the PB must contain a copy of the notice previously provided to the Contractor by the Client. The terms of calling the PB should be accurately recorded. The calling of the PB should only be undertaken by specifically authorised Client's personnel of suitable seniority. Normal remedies available under the contract should be applied, but not necessarily exhausted, before any use is made of a PB.

Client's bond -- the Contractor should consider asking for a PB to be provided by the Client, where this would be appropriate.

CONTRACT GUARANTEES AND BONDS (i)

FORM OF CONTRACT GUARANTEE

(To be completed on headed paper of Parent Company of Contractor)

Date

Dear Sirs,

CONTRACT FOR:

..... (“Company”) have entered into a Contract dated
and referenced(the “Contract”) with
..... (“Contractor”):

1. We, [*name of guarantor*], guarantee that [*name of Contractor*] shall duly perform all its obligations contained in the Contract.
2. If [*name of Contractor*] shall in any respect fail to perform any of its obligations under the Contract or shall commit any breach thereof, we undertake, on written notice by Company, to perform or to take whatever steps may be necessary to achieve performance of said obligations under the Contract and shall be responsible for any loss, damages, claims, costs and expenses which are incurred by Company by reason of any such failure or breach on the part of [*name of Contractor*] but only to the extent that such losses, damages, claims, cost and expenses are recoverable under the Contract. We also further reserve the ability to assert any claims or defences available to the Contractor.
3. Our guarantee and undertakings hereunder shall be unconditional and irrevocable, and without prejudice to the generality of the foregoing we shall not be released or discharged from our liability hereunder by
 - a. any waiver or forbearance by Company of or in respect of any of [*name of Contractor*]'s obligations under the Contract whether as to payment, time for performance or otherwise howsoever, or by any failure by Company to enforce the Contract or this instrument, or
 - b. any alteration to, addition to or deletion from the Contract or the scope of the work to be performed under the Contract, or
 - c. any change in the shareholding relationship between ourselves and [*name of Contractor*] and our guarantee and undertakings hereunder shall continue in force until all [*name of Contractor*]'s obligations under the Contract and all our obligations hereunder have been duly performed.

4. Notwithstanding anything express or implied to the contrary in the Contract or this Guarantee we shall not by virtue of this Guarantee acquire a total aggregate liability under this Guarantee in respect of the Contract which is greater than or of longer duration than that of [*name of Contractor*] under the Contract.
5. In the event Company or Contractor assigns a portion or the whole of the Contract to a third party, the Guarantor shall not be discharged from its liability under this Guarantee. [*See accompanying General Principles.*]
6. [*See accompanying General Principles re change of ownership of Contractor.*]
7. This document shall be governed by the laws of [*England and Wales*] and be subject to the exclusive jurisdiction of the [*English*] courts.
8. Any demand or notice by the Company to the Guarantor may be delivered personally to the Guarantor or sent to the Guarantor by post or facsimile transmission at the following

Address: [*Address of Contractor as stated in the Contract*]

For the attention of: [*Name of Contractor's Authorised Signatory*]

Facsimile: [*Contractor's Fax Number for Notices as stated in Contract*]

Any such notice or demand shall be deemed to have been received by the Guarantor forty eight (48) hours after posting (where sent by post) or immediately on delivery (where delivered personally or sent by facsimile transmission), exclusive of normally non-working days.

9. No third party may rely upon the terms of this Guarantee as if a party to this Guarantee.

Yours faithfully,

Signed: Director (Parent Company)

Name:

Date:

Signed: Director (Parent Company)

Name:

Date:

CONTRACT GUARANTEES AND BONDS (ii)

SIMPLE ON-DEMAND PERFORMANCE GUARANTEE/BOND

Our guarantee number:

.....

We are informed that:

.....

(hereinafter called the “Contractor”) has entered into a contract referenced

..... and dated with you

.....(Name of Client) and titled

..... (“Contract”) and that a guarantee for [*amount*] being % of the Contract price is required.

On behalf of the Contractor we [*Bank*] [*branch*] hereby give you our unconditional and irrevocable guarantee and undertake to pay you any amount or amounts not exceeding in total a maximum of [*amount*] on receipt of your first demand in writing over original handwritten signatures which written demand must contain a copy of the notice of default previously given by you to Contractor.

This guarantee shall continue in full force notwithstanding any alterations, additions or deletions to the Contract.

For the avoidance of doubt any document(s) received by way of facsimile or similar electronic means is/are not acceptable for any purpose(s) under this guarantee.

This guarantee is valid for written demands received by us on or before [*date*] after which date our liability to you under this guarantee will cease and this guarantee will be of no further effect.

This guarantee is personal to you and is not assignable.

This guarantee constitutes the entire agreement between us and you. No amendments to the guarantee shall be effective unless evidenced in writing and executed by us or unless this guarantee has been replaced by a similar guarantee.

This guarantee shall be governed by the Laws of [*England and Wales*] and be subject to the exclusive jurisdiction of the [*English*] courts.

CONTRACT GUARANTEES AND BONDS (iii)

CONDITIONAL ON-DEMAND PERFORMANCE GUARANTEE/BOND

Our guarantee number:

.....

We are informed that:

.....

(hereinafter called the “Contractor”) has entered into a contract referenced

..... and dated with you

..... (Name of Client) and titled

..... (“Contract”) and that a guarantee for [amount] being % of the Contract price is required.

On behalf of the Contractor we [Insurance Co] hereby give you our conditional and irrevocable guarantee and undertake to pay you any amount or amounts not exceeding in total a maximum of [amount] on receipt of your first demand in writing over original handwritten signatures provided. [Insert the condition(s) to be satisfied and any necessary verification of such satisfaction.]

This Guarantee shall continue in full force notwithstanding any alterations, additions or deletions to the Contract.

For the avoidance of doubt any document(s) received by way of facsimile or similar electronic means is/are not acceptable for any purpose(s) under this guarantee.

This guarantee is valid for written demands received by us on or before [date] after which date our liability to you under this guarantee will cease and this guarantee will be of no further effect.

This guarantee is personal to you and is not assignable.

This guarantee constitutes the entire agreement between us and you. No amendments to the guarantee shall be effective unless evidenced in writing and executed by us or unless this guarantee has been replaced by a similar guarantee.

This guarantee shall be governed by the Laws of [England and Wales] and be subject to the exclusive jurisdiction of the [English] courts.